MOST
MISSOURI'S 529 COLLEGE SAVINGS PLAN

CLINT ZWEIFEL
MISSOURI STATE TREASURER

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FROM: Bruce A. Ring, Jr.
Director of Investments

RE: 2013 Annual Program Review

Section 166.450 of the Revised Statutes of Missouri (RSMo) requires an annual review of the Missouri Higher Education Savings Program ("MOST") by the Director of Investments of Treasurer Zweifel's Office and the reporting of the findings to the Missouri Higher Education Savings Program Board ("Board"). The statute requires a review of five areas:

- Board administration
- Financial status
- Investment policy
- Participation rate
- Continued viability

Therefore, in accordance with these requirements, I am pleased to present the following findings from my review for calendar year 2013.

I. Board Administration

Ascensus Broker Dealer Services, Inc. (formerly Upromise Investments Inc.) assumed responsibility as program manager and Ascensus investment Advisors, LLC (formerly Upromise Investment Advisors, LLC) (together "Ascensus College Savings"), assumed responsibility as recordkeeping and servicing agent, for both the Direct and Advisor Plans on June 3, 2006. On February 7, 2011, the Board entered into another contract with Ascensus College Savings, following a Request for Proposal ("RFP") process. The new contract extends to June of 2016. The Board and Treasurer Zweifel's Office continue to work closely with Ascensus College Savings and monitor its management of the programs. In addition, the Board met quarterly during 2013, as required by law.

II. Financial Status

Following is a review of the financial status of our major partners and a summary of the investment performance of the most popular investment options within the MOST Plan.

A. Financial Status of MOST Partners

Financial markets in 2013 performed well across sectors and continued their upward trends in equities, while fixed income markets suffered a bit from rising interest rates. While the economy

is still struggling to recover, in general, the feeling is that there has been slow and steady progress in both economic and financial areas. While certain sectors like housing have shown signs of strength over the past year, the employment market is still sluggish.

On December 2, 2013, Ascensus, Inc., a privately held company, acquired Upromise Investments, Inc. and its affiliates Upromise Investment Advisors, LLC and Upromise Investments Recordkeeping Services, LLC (collectively the "Upromise Entities") from SLM Corporation (Sallie Mae). Effective May 14, 2014, the names of the Upromise Entities have changed as follows:

Prior Entity Name	**New Entity Name**
Upromise Investments, Inc.	Ascensus Broker Dealer Services, Inc.
Upromise Investment Advisors, LLC.	Ascensus Investment Advisors, LLC.
Upromise Investments Recordkeeping Services, LLC.	Ascensus College Savings Recordkeeping Services, LLC.

Upromise, Inc., which is no longer affiliated with the Ascensus College Savings companies, continues to offer the Upromise service under the name "Upromise."

The distributor for the Advisor Plan in 2013 is DeAWM Distributors, Inc (formerly known as DWS Investments Distributors, Inc.). DeAWM Distributors, Inc, is the retail distribution arm of Deutsche Asset and Wealth Management. As part of Deutsche Bank, DeAWM is responsible for managing approximately $1.2 trillion in active, passive and alternative assets globally for retail, institutional and high net-worth clients. Deutsche Bank is one of the world's largest global universal banks with total assets of $2.8 trillion, serving more than 31 million clients in 72 countries.   On August 11th, DeAWM completed its rebranding efforts by changing all fund names to Deutsche Funds. These changes will be reflected in marketing materials and the website viewed by advisors and participants going forward.

The investment manager for the Direct Plan in 2013, The Vanguard Group, remained a strong franchise. Vanguard is the world's largest mutual fund company and one of the world's largest investment management companies. Vanguard manages more than $2 trillion in global assets, including $281 billion in global ETF assets. The firm offers more than 160 funds to U.S. investors and more than 80 additional funds in non-U.S. markets. Within the 529 market, Vanguard is the largest provider of investments with $57.2B representing approximately 26% of the market.

B. Performance of MOST Underlying Funds

Overall, 2013 had a solid performance from equity and a more lackluster performance from fixed income. None of the fixed income funds showed positive results for the year while all of the equity funds showed positive results. Equity funds showed positive results ranging from 13.14% to 44.59%, while fixed income results ranged from -8.94% to -2.14%. The negative results for fixed income can be directly attributed to changes in the interest environment over the past 12 months.

The return for investment options in MOST, both Direct and Advisor was positive in all plan equity funds and underlying portfolios. The one-year returns of the funds in the Direct Plan,

excluding the Interest Accumulation Portfolio ranged from -3.39% (Vanguard Conservative Income Portfolio) to +44.10% (Vanguard Explorer Fund Admiral). The returns for all options in the Advisor Plan were similar with a range of -10.18% for the lowest one year return (American Century Inflation Adjusted Bond) and +40.21% (Columbia Small Cap Index Fund) for the best performer. Underlying fund performance was similar in that all funds showed similar positive returns for the year. Funds with an international component generally outperformed those with only a domestic exposure.

Treasurer Zweifel's office is responsible for monitoring the relative performance of each of the underlying investment alternatives versus an established benchmark. This effectively measures the contribution that the investment manager's expertise has on participants' returns. Despite good absolute returns, primarily in equity, for the calendar year, relative performance for most of the funds (6 Direct and 9 Advisor) can best be described as at or below benchmark for the period. While Index funds are expected to be at or below benchmark, depending on the extent to which they stray from exact matching of the index, actively managed funds are expected to exceed those benchmarks. To summarize, the investment managers' overall contribution to participants' returns was negative, albeit modestly. As of year-end, three advisor funds were on the Watch List for negative intermediate-term performance results. All passive (index tracking) funds performed satisfactorily, and experienced low tracking error of returns versus their relevant indices.

III. Investment Policy

The Missouri Higher Education Savings Program Board adopted a formal investment policy, governing program investments, in mid-2007. The policy establishes objectives for structuring the investment options in the Direct and Advisor Plan, formulates policies for selecting appropriate investment managers and the use of specific investment vehicles, and establishes an investment performance process for underlying funds in the Plan. The policy is an important statement by the Board in terms of defining its fiduciary responsibilities and standards for Treasurer Zweifel's office staff and MOST partners. The policy was modified in 2008 to allow the Director of Investments, rather than the Board, to make the decision to place or release a fund to/from "WATCH" status. The Board again modified the investment policy in August 2011 to provide that the formal review period for a fund would be three consecutive quarters (as opposed to two consecutive quarters) when looking at benchmark performance evaluation for the Watch List. "Beta" and "Alpha" measures were also added to the review process for funds when determining Watch List eligibility and quarterly performance, as well as the elimination of the "value of active management" measurement criteria. The investment policy was reviewed but not changed during 2013.

IV. Participation Rate

Following is an examination of the participation rate of the MOST program. By examining the participation rate for the program, we can attempt to gauge the relative success the program has had in reaching the state's residents and encouraging them to increase college savings—the original goal of the IRS section authorizing these programs. The relative success or failure of states' various 529 programs rests on many different factors including the effectiveness of marketing efforts, availability of a state tax deduction, demographic and economic conditions, cost structure and the abilities and resources of states' partners to attract and retain assets.

However, one facet that has remained a constant is the competition for assets among states' program managers. As the field of firms in the 529 industry has shrunk, this competition for assets remains fierce as evidenced by the decline in fees among plans issuing new RFP's in recent years.

A. Growth of Plan in 2013

The MOST Plans experienced growth in both assets and accounts during the year 2013. The asset growth in 2013 is due to both investment returns and increased contributions, while the positive change in number of accounts is primarily the result of plan marketing, increased awareness, and popularity of the program.

Combined Plan assets grew by a rate of 17.3% as compared to a 15.2% growth rate last year, ending the year at approximately $2.277 billion as compared to year-end 2012 at $1.941 billion. Growth was experienced in both the Advisor (21.48%) and the Direct Plans (16.8%) although the majority of the absolute dollar growth was again accounted for in the Direct Plan. Both plans grew at a higher rate than the two prior years which saw Advisor Plan growth at 19.9 % and 7% respectively, and Direct Plan growth at 14.8% and 5.2% for years 2012 and 2011. For the past three years, plan growth in MOST has been driven by market returns and to a lesser extent, account growth.

Contributions during the period once again outpaced withdrawals, also contributing to the positive asset growth. Total combined contributions for both plans equaled $266.2 million, while withdrawals were $194.3 million. Contributions increased by $13.1 million in 2013 versus $26.2 million in 2012 and $7 million in 2011. A general increase in contributions should be expected as the economy continues to recover and the cost of higher education increases.

The number of accounts grew by a rate of 4.7%, the rate of growth increasing from a year earlier (3.3%), resulting in a total of 142,859 combined accounts at year-end. The rate of growth for the Advisor Plan was 2.5% and the Direct Plan was 4.5%. Roughly 88% of account holders are Missouri residents, an amount relatively unchanged in 2013.

B. Comparison of MOST Participation to National Trends

Nationally, assets in 529 Plans on average have grown significantly over the past decade, but at a decreasing rate. Similar to Missouri, levels plummeted in 2008 due primarily to the financial market performance, but accounts have continued to grow signaling that popularity and awareness across the country is on the rise. Overall, the growth trends for Missouri's MOST Plan, both in respect to assets and accounts, have consistently mirrored the national rates over the past several years. In 2013 MOST assets increased by 17.3%, slightly behind the national rate of 21.3%

The 529 Plan landscape is a maturing marketplace and several trends are emerging. Most noticeably is the rise in competition and its impact on program fees. Many states are re-bidding their plans and this is accelerating the fee reduction impact. As a result, some program managers are even voluntarily reducing fees in a pro-active effort to improve client retention. Innovative and cost-effective market initiatives, as well as more conservative investment options such as CDs, are also prominent trends in the 529 market. Remaining at the forefront of these market trends will be critical to the success and competitiveness of Missouri's MOST program in coming years.

MOST's program management contract with Ascensus College Savings (formerly Upromise Investments and Upromise Investment Advisors) was renewed in 2011. Some fairly significant changes to the Advisor Plan were put into place in 2011. These changes included the elimination of some poor performing funds and the addition of DWS as a partner in the Advisor Plan. DWS brings with it a broad family of plans as well as a significant relationship with the Broker-Dealer community which should continue to improve our visibility with this all important aspect of the Advisor Plan.

V. Continued Viability

The MOST program remains a viable college savings program. In Ascensus College Savings' seven and one-half years of program management we have experienced strong trends in asset and account growth despite the market turmoil that plagued much of this period. We also saw an upswing in the number of new beneficiaries enrolled in the plan, which shows growth of new customers, and much better participation in the Advisor Plan among Missouri-based brokers over the past year.

The performance of the Plan throughout the economic downturn and subsequent recovery has been resilient. The fact that participants weren't required to make non-qualified withdrawals on a large scale during this period is promising. As a result, the majority of participants should have experienced almost full recovery of their college savings account balances. The economic environment remains challenging, but the view in regard to a sustainable recovery and financial markets stability is one of optimism. With this outlook, we should expect to see growth in all aspects of the plans continue. Increased competition in the 529 marketplace requires innovation and a commitment to excellence to ensure MOST continues to grow.

Missouri's MOST 529 Plan remains not only viable, but well positioned for growth as one of the premiere plans in the country.